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ECONOMIC TALKING POINTS

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The Fed Should Stop Fretting About An "Unsustainable Hot" Job Market

Let's begin with April's employment numbers and then later bring up why, I believe, the Fed wrongly uses this data to carry out its current monetary policy.

First, we saw another solid increase in payrolls last month, with employers adding an additional 428,000 workers. Such hiring has been averaging nearly 519,000 a month since the start of the year—–this despite the fact labor productivity itself has collapsed in this first quarter by the most since 1947.

Ironically, despite this dismal productivity, average hourly earnings still managed to increase by 5.5% last month, the second largest annual increase in 14 months. The fact that pay has held up this well is interesting, especially since average weekly hours worked has been trending down since the start of 2021.

On the whole, the establishment survey shows labor market conditions continuing to improve, with manufacturing employment adding 55,000, and leisure and hospitality posting another 78,000 to payrolls last month.

I had hoped to find at least some corroboration of these upbeat data points in the household survey, but didn't quite get it. Here, the total number of people employed in the US actually plummeted by 353,000 last month, with

363,000 dropping out of the labor force completely. Because of these two figures, the unemployment rate held at 3.6%.

So what is it about the job numbers that raises fresh concerns about the present course of Fed monetary tightening?

First, there appears to be a tendency by the Fed to pick and choose data points that essentially highlight the strength of the labor market to justify ramping up the pace of monetary tightening. Whether that is a valid criticism or not is arguable. But as an economist, I must say it always sounds bizarre to hear Fed chair Powell — or any government official — claim the job market is too strong! Or as Powell put it, the current labor market is "too hot," even "unsustainably hot."

Such sentiments have an odd ring to them. Policymakers typically strive to create a backdrop that maximizes employment. With more people at work, the less the government spends on jobless benefits, the larger the tax base, and there's ample research to show low joblessness also reduces crime. It's a total win – win situation.

Yet the Fed today views the exceptional strength in the labor market as a significant source of inflation — and thus needs to be tamped down with higher interest rates.

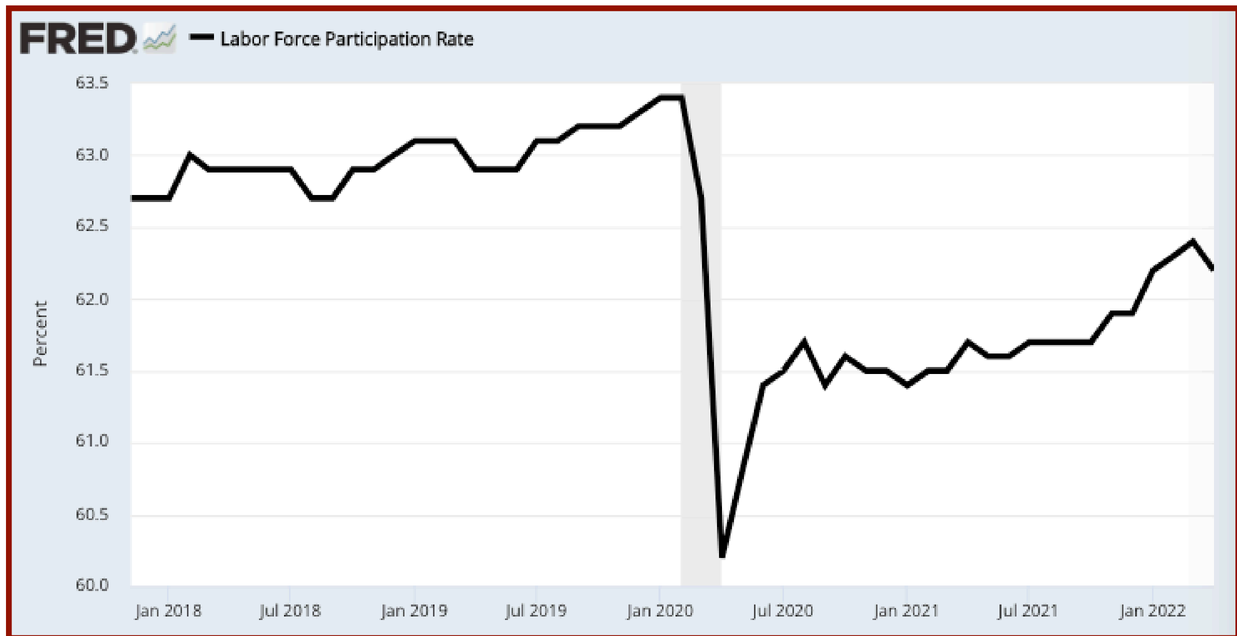
But the villain here is not the strength in U.S. hiring. If anything, the robust growth in jobs serves as a way to help increase the output of goods and services — and thus cool inflation pressures.

Look, I understand the Fed's rationale. Companies are in fierce competition to fill some 11.5 million vacancies at a time when there are less than 6 million people jobless who are actively seeking work. Fed economists worry that efforts to attract this limited pool of unemployed workers, as well as retain existing staff, will keep driving wages higher, which then forces employers to pass higher labor costs on to consumers. The subsequent jump in the cost of living would have employees demand even more pay increases and in the process ignite what the Fed fears most of all — a destructive wage and price spiral. At least these were the predominant linkages for much of the post world War II era.

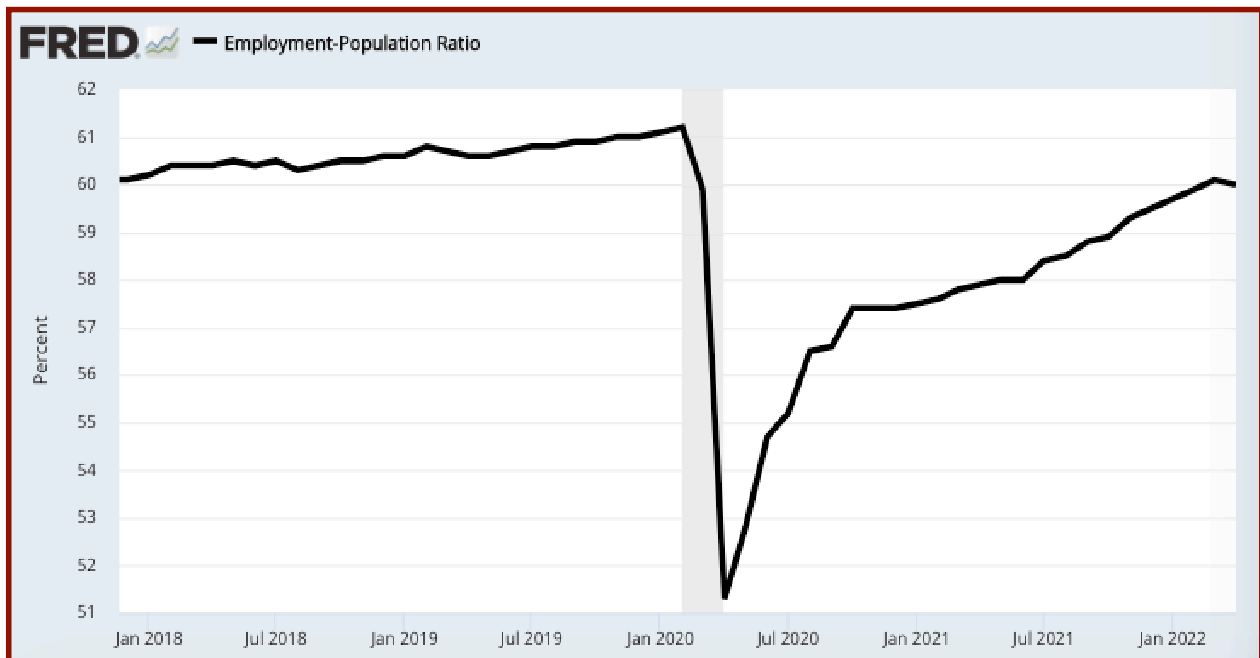
But I think we have to upgrade our understanding of economics to identify who really is the villain in the current inflation story. Should we really put the brakes on the economy and reduce price pressures by suppressing job creation? I don't think so. Technology, robotics, AI and cyber security have spawn millions of new jobs to help the economy function much more efficiently.

The real villain is that we do not have adequate policies in place to increase the supply of qualified workers.

For example, I find it strange the Fed would point to an overheating job market when April's labor force participation rate at 62.2% is still short of the 63.4% we saw before the onset of the pandemic (February 2020).



And the employment - population ratio just slipped last month to 60%, considerably below the 61.2% in Feb. 2020. Do these latest figures really reflect an overheated job market?



And I also find it peculiar why annual pay increases of 5.5% is so alarming to the Fed when even that pace is insufficient to keep up with inflation. This ongoing erosion in household purchasing power should itself cool demand in the economy.

Nor do I see much evidence that we're in a unique period of excessive domestic spending. The growth in real personal consumption expenditures in the first quarter was really no different than what it was in the years prior to the pandemic!

Sure, you might counter that this is precisely the problem. Consumer spending may not have changed much but the fallout from Covid, the war in Ukraine and the China's lockdowns of major cities and ports to control viral outbreaks unfortunately caused severe global scarcities in critical goods. So domestic demand is chasing fewer supplies and thus driving up prices.

I get that, but the Fed has little control over the latter. For the Fed to aggressively raise rates and thus subvert job creation and wage growth just to keep domestic spending in better balance with global supplies seems like pre-21th century economics and a certain path to recession.

The two points I am making is this: first, the labor market does not appear to be as "hot" as Powell claims and any effort to restrict its growth would only restrain the kind of domestic production that can help offset the shortage in basic commodities.

Second, if you want to increase the supply of labor, Congress has to take a more assertive role in loosening up immigration policies (e.g., H2B visas) and allocate more funds and/or tax credits to facilitate the training of jobless Americans so they can acquire the skills that are in demand these days, whether it be for software engineers or truck drivers.

The strong job market should be viewed as an asset for the U.S. economy, not a liability.

United States

	I 2021	II 2021	III 2021	IV 2021	I 2022	II 2022	III 2022	IV 2022	I 2023	II 2023	III 2023	IV 2023	I 2024	II 2024	III 2024	IV 2024
Real Gross Domestic Product (GDP):																
%	6.3	6.7	2.3	6.9	-1.4	3.3	2.8	2.6	1.8	3.6	3.1	2.1	2.4	3.3	2.4	2.8
Personal Consumption Expenditures:																
PCE %	11.4	12.0	2.0	2.5	2.7	3.8	2.6	2.0	2.1	4.1	3.2	2.0	2.6	3.8	2.6	2.7
Inflation, end of period, year-over-year:																
CPI %	2.6	5.3	5.4	7.0	8.5	8.8	7.4	4.1	3.3	2.8	2.6	2.3	2.2	2.3	2.3	2.4
Unemployment Rate (end of period):																
%	6.0	5.9	4.7	3.9	3.6	3.5	3.4	3.4	3.6	3.7	3.6	3.5	3.7	3.6	3.6	3.5
Non-farm Payrolls, monthly avg. thousand:																
	513	615	651	365	562	445	465	340	385	510	495	410	275	310	315	325
Treasury 10-yr Note Yield % (end of period):																
	1.75	1.44	1.52	1.51	2.32	2.80	2.70	2.55	2.55	2.70	2.70	2.60	2.65	2.61	2.72	2.70
Federal funds rate % (end of period):																
	0.13	0.13	0.13	0.13	0.38	1.13	1.63	2.13	2.38	2.38	2.38	2.38	2.38	2.38	2.38	2.38

GDP Growth - Global Economy - Year over Year

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
US	2.6	1.6	2.2	1.8	2.3	2.7	1.7	2.3	2.9	2.3	-3.4	5.7	2.2	2.4	2.7
Eurozone	1.7	1.4	-0.9	-0.2	1.4	2.1	1.9	2.5	1.9	1.2	-6.7	5.2	1.8	2.4	2.5
United Kingdom	1.7	0.7	0.3	1.8	2.9	2.2	1.9	1.9	1.3	1.5	-9.8	7.5	3.3	2.4	2.3
Japan	4.6	-0.4	1.6	1.5	-0.1	1.1	0.5	1.7	0.6	-0.2	-4.5	1.7	2.0	2.2	1.9
Canada	3.1	3.1	1.8	2.3	2.9	0.7	1.0	3.2	2.0	1.6	-5.3	4.5	3.0	2.9	2.6
India	8.4	8.6	6.7	4.9	7.4	8.0	8.1	7.2	6.8	4.8	-7.5	9.2	6.6	6.8	6.9
China	10.5	9.5	7.8	7.7	7.3	6.9	6.7	6.8	6.6	6.1	2.2	8.1	4.3	5.5	5.6
Brazil	7.5	2.7	0.9	2.3	0.1	-3.5	-3.5	1.2	1.2	1.1	-3.9	4.5	1.6	2.2	2.6
Mexico	5.2	4.0	3.9	1.4	2.3	2.7	2.7	2.4	2.1	-0.1	-8.5	5.0	1.9	2.6	2.4
Australia	2.8	2.6	3.6	2.4	2.6	2.5	2.4	2.4	2.7	1.8	-1.1	4.7	3.8	2.7	2.9
Russia	4.0	4.3	3.4	1.3	0.6	-2.8	-0.2	1.6	2.5	1.2	-2.9	4.5	-14.0	-5.0	2.1
World	4.2	3.1	2.5	2.6	2.8	2.8	2.6	3.4	3.2	2.7	–3.1	6.1	3.4	3.9	4.1

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